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No. 226

In the Supreme Court of the United States

OCTOBER TERM, 1958

GENERAL PUBLIC UTILITIES CORPORATION, AS COMMON PARENT CORPORATION OF AN AFFILIATED GROUP OF CORPORATIONS, ET AL., PETITIONERS,

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

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OPINIONS BELOW

The Court of Claims did not enter an opinion herein, but dismissed the taxpayers' petition "on the basis of the facts as stipulated by the parties and the decision of this date in *Atlantic City Electric Company* v. *United States*, No. 33-55 * * *." (Pet. 17.) The opinion of the Court of Claims in *Atlantic City Electric Co.* v. *United States* (Pet. 18-28) is reported at 161 F. Supp. 811.[1]

[1] Taxpayer in the *Atlantic City* case filed a petition for a writ of certiorari on August 4, 1958 (No. 251, this Term).

JURISDICTION

The order of the Court of Claims dismissing taxpayers' petition was entered on May 7, 1958. (Pet. 17.) Taxpayers' petition for a writ of certiorari was filed on July 26, 1958. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1255(1).

QUESTION PRESENTED

Whether the Court of Claims erred in holding that the premium paid by a public utility corporation on the redemption of its preferred stock was not a "dividend" within the meaning of Section 26(h) of the Internal Revenue Code of 1939, and hence did not qualify for the dividends-paid credit allowed by that provision of the Code.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra*, pp. 17-22.

STATEMENT

The material facts, as stipulated by the parties (Pet. 36-41), may be summarized as follows:

General Public Utilities Corporation (GPU) is a New York corporation engaged in business as a public utility holding company. During 1947, GPU was the parent of an affiliated group of corporations, as defined in Section 141 of the Internal Revenue Code of 1939, and this group included New York State Electric & Gas Corporation (hereafter called New York State) and the other taxpayers herein. (Pet. 36-37.)

In 1941, taxpayer New York State issued and sold 120,000 shares of 5.10% cumulative preferred stock of a par value of $100 per share, redeemable at $105 per share, for a price of $100.85 per share or an aggregate

amount of $12,102,000. New York State was a "public utility" and its 5.10% cumulative preferred was "preferred stock" within the meaning of those terms in Section 26(h) of the 1939 Code. New York State's expenses of issuance and sale amounted to $47,753.99, of which $6,561.92 was stamp tax allowed as a deduction in determining the corporation's 1941 federal income tax. (Pet. 38-39, 41.)

In 1947, taxpayer New York State redeemed the 120,000 shares of 5.10% cumulative preferred issued and sold in 1941, paying the redemption price of $105 per share plus accrued dividends of $20,400, or an aggregate of $12,620,400. The aggregate amount thus paid exceeded by $539,192.07 the amount New York State had received on the issuance of the cumulative preferred, after deducting $41,192.07 of issuance expenses for which no deduction from income had theretofore been claimed or allowed in determining the corporation's federal income tax liability. (Pet. 40-41.)

In December, 1946, taxpayer New York State debited earned surplus in the amount of $1,204,211.78 and credited other reserves with this amount. As of December 31, 1946, the books of the corporation disclosed an earned surplus of zero. During the year 1947, the corporation had net taxable income of $5,172,048.82, and distributed dividends on all its stock (exclusive of the accrued dividends of $20,400 paid in connection with the redemption of the 5.10% preferred) aggregating $3,210,009.30. At the end of 1947, the corporation had earnings and profits, after taking into account all items affecting earnings and profits for such year other than the redemption of 5.10% preferred, of not less than $1,000,000. (Pet. 39-40.)

In connection with the issuance and sale of the 5.10% preferred, New York State's book entries credited capital stock account $12,000,000, credited premiums on capital stock $102,000, and charged capital stock expense account $47,753.99. On redemption of the stock, New York State charged capital stock account $12,000,000, charged premiums on capital stock $102,000, credited capital stock expense account $47,753.99, and charged reserve for charges connected with refinancing account $600,000 on account of the stock issuance, sales expenses, and payment of redemption premium on the preferred stock. (Pet. 41.)[2]

On auditing taxpayers' consolidated return for 1947, the Commissioner disallowed in full a credit in the amount of $600,000 against income, claimed by taxpayers under Section 26(h) of the 1939 Code by reason of the payments made by New York State to its stockholders in the redemption of its 5.10% cumulative preferred. Thereafter, on behalf of the affiliated group, GPU filed a claim for refund of 1947 taxes theretofore paid, on the ground that the Commissioner erred in failing to allow a credit of $539,192.07 under Section 26(h). The Commissioner disallowed the refund claim, and the instant litigation ensued. (Pet. 38.)

ARGUMENT

Section 26(h)(1) of the 1939 Code, App., *infra*, p. 17, provides a special credit against the income of "a public utility" for "dividends paid during the tax-

[2] On the basis of these stipulated facts, it would appear that taxpayer errs in stating that (Pet. 4) "The excess amount paid in redemption of its 5.10% cumulative preferred stock was, in fact, charged to earned surplus on New York State's books (S. Pars. 13 and 20 and Exhibit J.)"

able year on its preferred stock." The ultimate question here is whether a premium paid by taxpayer New York State on the redemption of an issue of preferred stock qualifies for this dividends paid credit.[3] It is stipulated that New York State was "a public utility" and that the preferred stock redeemed was "preferred stock" within the meaning of Section 26(h). (Pet. 41.) Hence the dispositive issue is whether the premium paid on redemption constituted "dividends paid" within the meaning of the statute. The Court of Claims answered this question in the negative. In seeking review by this Court, taxpayers do not, and can not, assert a conflict. They rely principally upon asserted Congressional intention which they infer (except as to Section 26(h)) from the legislative history underlying the relevant provisions of the Code. (Pet. 5-6, 8-10.) Taxpayers' reliance is misplaced. As demonstrated below, the statutory constructions urged by them are refuted by the express language of the relevant provisions, by legislative history, by a series of decided cases which taxpayers mention (Pet. 14) but fail to discuss, and by other relevant considerations.

1. While Section 26(h) contains express definitions of the terms "public utility" and "preferred stock" as used therein, it allows a credit for "dividends paid" without defining "dividends." On the face of the statute, then, the term "dividends" is not used in any special sense; its meaning must be determined by reference to Section 115 of the Code. App., *infra*, pp. 20-22.

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[3] Although taxpayers originally claimed a credit for the entire amount of the premium paid on redemption of the stock ($600,000), taxpayers have reduced the amount claimed to $539,192.07 through adjustments for various items detailed in the Statement. (Pet. 3-4, 38.)

which is the basic provision governing the nature of corporate distributions for federal tax purposes. Taxpayers, however, seek to avoid this cross-reference (Pet. 5-6) by asserting that the intention of Congress in enacting Section 26(h) requires the extension of the "dividends paid" credit to redemption premiums. Their argument on this point, which contains no discussion of legislative history, is unsound. Section 26(h) was first enacted by Section 133 of the Revenue Act of 1942, c. 619, 56 Stat. 798, 830, and while the Committee Reports are not illuminating, the extensive hearings on this provision afford considerable insight.[4] These Hearings reveal that representatives of public utility companies urged the allowance of a dividends paid credit on preferred stock because the Securities and Exchange Commission was requiring public utilities to maintain a substantial portion of their capital in the form of preferred stock as opposed to bonds. Significantly, they asked for the credit *only* as to dividends paid on *cumulative* preferred stock, emphasizing that such dividends were *recurrent* fixed charges which had to be paid before common stockholders could receive dividends, and hence were similar in character to periodic interest payments on bonds. Senators Barkley and Guffey indicated their approval of this limited analogy (1 Senate Hearings, Revenue Revision of 1942, pp. 159, 160-163), and Section 26(h), as enacted, allows only what the proponents asked for, i.e., a credit for "dividends paid" on *cumulative* preferred stock;

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[4] 1 House Hearings, Revenue Revision of 1942, pp. 199, 203; 3 House Hearings, Revenue Revision of 1942 pp. 3327, 3331, 3334; 1 Senate Hearings, Revenue Revision of 1942, pp. 159, 160-161; 2 Senate Hearings, Revenue Revision of 1942 pp. 1813, 1815, 1839, 1845, 1859, 1869, 1872, 1873, 1876, 1888, 2307, 2308.

neither noncumulative nor participating preferred stock would qualify under Section 26(h)(2)(B).

Manifestly, redemption premiums are not the fixed, recurrent charges, payable in preference to common stock dividends, which constitute the sort of dividends analogized in the Congressional hearings to interest payments on bonds. Rather, redemption premiums are payments to be made only once, at the option of the corporation. The very object of redemption is to terminate stock ownership and the concomitant right to recurrent dividends. Indeed, that Section 26(h) is focussed upon recurrent dividends; paid in the ordinary course of business to continuing shareholders, is implicitly confirmed by the statutory limitation to dividends paid *on* preferred stock *during* the taxable year. The fact that bond premium and discount can be amortized is not material. Congress was not asked to put preferred stock on a par with bonds in all respects; there is no evidence that it intended to do so; and, indeed, the language of Section 26(h) is inconsistent with such an intention.

2. Taxpayers' second contention (Pet. 7-10) is that their claim to a credit for "dividends" paid is sustained by cross-reference to Section 115 which, as noted, governs the nature of corporate distributions for tax purposes generally. Taxpayers do not dispute that the corporate distribution here involved was a distribution in liquidation as defined by Section 115(c) and (i), App., *infra*, pp. 20-22. Nevertheless, while Section 115(c) specifically requires that distributions in liquidation "shall be treated" as payments in exchange for stock, taxpayers argue that this requirement of Section 115(c) is addressed only to stockholder-distributees,

and hence that it is only such distributees who must treat the transaction as a sale of their stock giving rise to capital gain or loss. The distributing corporation, according to taxpayers, is favored with different treatment because the last sentence of Section 115(c) provides that the part of a liquidating distribution properly chargeable to capital account shall not be considered a distribution of earnings or profits. Since this provision implies its converse—a charge against earnings and profits where capital account is not properly chargeable—taxpayers argue that it constitutes, in effect, a *renvoi* for the distributing corporation to Section 115(a) and (b), which broadly define a "dividend" as every corporate distribution to the extent of post-1913 earnings and profits.

However, the first sentence of Section 115(c) provides unequivocally and without qualification that a distribution in liquidation "shall be treated" as payment in exchange for stock. This surely characterizes a redemption of stock as a capital transaction—a sale by the stockholder-distributee and a purchase by the corporate distributor. It is true that the closing sentence of Section 115(c) contemplates that liquidating distributions may, in part, be charged against earnings and profits on the books of the corporation. But this provision was added in 1924 to the predecessor of Section 115(c) for the limited purpose—stated both in the original statutory language and its legislative history—of determining the level of earnings and profits available for *future* distributions.[5] Twelve years later, in the Revenue Act of 1936, c. 690,

[5] Section 201(c) of the Revenue Act of 1924, c. 234, 43 Stat. 253, 255; S. Rep. No. 398, 68th Cong., 1st Sess., pp. 11-12 (1939-1 Cum. Bull. (Part 2) 266, 274).

49 Stat. 1648, 1687-1688. Section 115(c), this explicit declaration of limited purpose was omitted from the statute. The Committee Reports are silent concerning this omission,[6] and the reasonable assumption is that the language was dropped as surplusage—not that Congress intended any substantive change. Moreover, Congress has expressly prescribed, in Section 115(g), that a distribution in redemption of stock shall be treated as a taxable dividend to the extent of available earnings and profits *only* if the distribution is made at such time and in such manner as to be essentially equivalent to a dividend. There is no distinction here between the distributing corporation and the stockholder-distributees; and the tests of dividend equivalence elaborated by the courts do not suggest any such distinction. See, *e.g., Rheinstrom* v. *Commr.*, 125 F. 2d 790 (C.A. 6th), certiorari denied, 317 U.S. 654.

This is the clear statutory scheme and it is one of long standing. The changes over the years stressed by taxpayers (Pet. 8-9) are immaterial here. The central fact is that the treatment of liquidating distributions as payments in exchange for stock has been continuously in effect since 1924, when it was embodied in Section 201(c) of the Revenue Act of 1924, c. 234, 43 Stat. 253, as an exception to the broad definition of "dividend" in Section 201(a). The underlying Senate Report said:[7]

> A liquidating dividend is, in effect, a sale by the stockholder of his stock to the corporation * * *.

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[6] H. Rep. No. 2475, 74th Cong., 2d Sess. (1939-1 Cum. Bull. (Part 2) 667); S. Rep. No. 2156, 74th Cong., 2d Sess. (1939-1 Cum. Bull. (Part 2) 678).

[7] S. Rep. No. 398, 68th Cong., 1st Sess., pp. 11-12 (1939-1 Cum. Bul. (Part 2) 266, 274).

> Treating such a transaction as a sale and within the capital gain provisions is consistent with the entire theory of the Act and, furthermore, is the only method of treating such distributions which can be easily administered.

The House Report also characterized this as "the true effect" of such distributions.[8] Neither in these reports, in the statutory language in effect since 1924, nor in subsequent legislative history is there any qualification of this realistic approach—or any suggestion that a distribution in stock redemption can at one and the same time be treated as a sale by the stockholder-distributees, and as something else (i.e., a "dividend" distribution) by the distributing corporation. If a stock redemption is to be a "dividend," it must meet the dividend equivalence tests under Section 115(g), and if it meets those tests it is a "dividend" both as to distributees and as to distributor.

The Code provides further confirmation that Section 115(c) precludes "dividend" treatment of liquidating distributions, by either distributor or distributees, absent a specific exception such as that provided by Section 115(g). Section 27(a) and (b), App., *infra*, pp. 18-19, allow a credit for "dividends paid," by certain corporations, including, *inter alia*, personal holding companies and companies unreasonably accumulating surplus. Section 27(g), App., *infra*, p. 19, qualifies that allowance as follows:

> In the case of amounts distributed in liquidation the part of such distribution which is properly

[8] H. Rep. No. 179, 68th Cong., 1st Sess., p. 11 (1939-1 Cum. Bull. (Part 2) 241, 249).

chargeable to the earnings or profits accumulated after February 28, 1913, shall, *for the purposes of computing the basic surtax credit under this section*, be treated as a taxable dividend paid. [Italics supplied.]

Obviously, this provision would have been unnecessary if the portion of a liquidating distribution chargeable to earnings and profits, under the last sentence of Section 115(c), automatically constituted a "dividend" under Section 115(a) as to the corporate distributor. If this were true, Section 27(a) and (b) would have sufficed to give the distributor the "dividends paid" credit for such portion of every liquidating distribution. Moreover, Section 27(g) is expressly limited in scope to the credit allowed under Section 27. And it is significant that Section 26(h), the "dividends paid" credit provision upon which taxpayers rely in the case at bar, contains no such proviso with respect to liquidating distributions—although the predecessor of Section 27(g)[9] was enacted five years before Section 26(h) was added to the Code. And, Section 26(h) has its complement within the same section, i.e., subsection (b), which allows credits for "dividends received." Surely, Congress did not intend the term "dividends" to have one meaning in subsection (b) and another in subsection (h). When it did intend a special scope for "dividends paid," as distinct from "dividends received," it expressly defined that scope in Section 27(g), as we have seen.

3. That liquidating distributions are governed exclusively by Section 115(c), and cannot constitute "dividends" under Section 115(a) from any point of view.

[9] Section 27(f) of the Revenue Act of 1936, c. 690, 49 Stat. 1648.

has long been the administrative position of the Treasury. Article 1548 of Treasury Regulations 45 (1920 ed.) categorically declared that "So-called liquidation or dissolution dividends are not dividends within the meaning of the statute * * *." Subsequent Regulations have, without exception, strictly adhered to this basic distinction. Section 29.115-1 of Treasury Regulations 111, as amended by T.D. 5377, 1944 Cum. Bull. 257, promulgated under the 1939 Code, provides: "The term 'dividend' does not include distributions under section 115(c), relating to distributions in liquidation * * *."

This long-standing and consistent administrative position was approved by this Court as early as 1928, in *Hellmich* v. *Hellman*, 276 U.S. 233, where it was held that a liquidating distribution could not qualify as a "dividend" under the 1918 counterpart of Section 115 (a),[10] regardless of available earnings and profits, because (p. 237):

> it was intended that such distributions should be governed by § 201(c), which, dealing specifically with such liquidation, provided that the amounts distributed should "be treated as payments in exchange for stock" * * *. The Treasury Regulations correctly interpreted the Act as making § 201(a) applicable to a distribution made by a going corporation to its stockholders in the ordinary course of business, and § 201(c) applicable to a distribution made to stockholders in liquidation of the corporation.

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[10] Section 201(a) of the Revenue Act of 1918, c. 18, 40 Stat. 1057, 1059. Section 201(c) of that Act was the earliest precursor of Section 115(c).

The Court did not regard this specific exclusion of liquidating distributions from the broad definition of "dividend" as an exclusion limited to the predecessor of Section 115. To the contrary, it obviously regarded the distinction as pervading the entire Revenue Act. The ultimate question presented was whether a liquidating distribution could qualify as a "dividend" for the purposes of the dividends-received credit allowed by Section 216(a), and the Court held that it could not, because the predecessor of Section 115(c) was controlling.

4. The holding and rationale of *Hellman* have been repeatedly invoked in a series of later decisions dealing with claims by corporate distributors for credits under the provisions of 1939 Code Section 27, discussed above. Section 27(a) and (b) prescribe the computation of a credit for "dividends paid," but—like Section 216(a) of the 1918 Act, involved in *Hellman*, and Section 26(h) of the 1939 Code, involved in the case at bar—Section 27(a) and (b) do not define the term "dividends." Two decisions are particularly significant here—*St. Louis Co.* v. *United States*, 237 F. 2d 151 (C.A. 3d), certiorari denied, 352 U.S. 1001, and *Shellabarger Grain Products Co.* v. *Comissioner*, 146 F. 2d 177 (C.A. 7th). In these cases, the taxpayers made exactly the same contention with respect to Section 27(a) and (b) that the taxpayer in the instant case makes with respect to Section 26(h).[11] They contended that,

[11] *St. Louis Co.* dealt with the provisions of the 1939 Code, while *Shellabarger* dealt with the predecessor provisions of the Revenue Act of 1936, *supra*. For convenience here, the cases are discussed together in terms of the provisions of the 1939 Code. Except for the fact that Section 27(g) of the 1939 Code constituted Section 27(f) of the 1936 Act, the provisions appeared under identically numbered and lettered sections and subsections.

for the purpose of determining whether a liquidating distribution constituted a "dividend" under Section 27(a) and (b), the distribution should be tested against the broad definition of "dividend" in Section 115(a) —without regard to the provisions of Section 115(c). Hence, they argued that with respect to all corporate distributions they were entitled to a credit to the full extent of accumulated and current earnings and profits. The Third and Seventh Circuits rejected these arguments; invoking *Hellman*, they held that, since Section 115(c) precluded a liquidating distribution from qualifying as a "dividend" under Section 115(a), it followed that such a distribution could not qualify as a "dividend" for the purposes of the dividends-paid credit under Section 27(a) and (b). The courts concluded, therefore, that the taxpayers were entitled only to the special credit with respect to liquidating distributions allowed by Section 27(g), discussed above, which provides that the portion of a liquidating distribution properly *chargeable* to earnings and profits shall be *treated* as a taxable dividend.

This Court too has recognized that it is only by virtue of the express provisions of Section 27(g) that a corporate taxpayer may properly claim a dividends-paid credit with respect to a liquidating distribution under Section 27. Thus, in *Helvering* v. *Credit Alliance Corp.*, 316 U.S. 107, dealing with the predecessor of Section 27(g), this Court stated (p. 110):

> Although a distribution in liquidation of earnings which accrued subsequently to February 28, 1913, does not constitute a dividend in the proper sense of the term, * * * [citing *Hellmich* v. *Hellman*,

supra], subsection (f) categorically declares that a liquidating distribution, to the extent it is composed of such earnings, shall, for the purposes of computing the dividends-paid credit "*be treated as a taxable dividend paid.*" [Court's own italics.]

We submit that these decisions, together with the clear statutory scheme and the long-standing and consistent administrative position of the Treasury, allow only one conclusion:—that a liquidating distribution cannot constitute a "dividend" under Section 115(a), because it is controlled by Section 115(c), and therefore cannot qualify for the "dividends-paid" credit under Section 26(h), any more than it could qualify for the "dividends-paid" credit under Section 27(a) and (b), or the "dividends-received" credit under Section 216(a) of the 1918 Act. In short, a liquidating distribution cannot be treated as a dividend for any purpose whatsoever, absent an express statutory exception to Section 115(c)—such as Section 27(g), or Section 115(g), which governs stock redemptions essentially equivalent to a dividend.

5. Since, as shown above, the decision below is clearly correct, and there is no conflict, there is no merit to taxpayers' contention (Pet. 11-15) that this Court should grant their petition because the question involved is important to many public utilities, and is involved in other pending cases. Whether a conflict may ultimately develop in decisions hereafter rendered by lower courts, as taxpayers hopefully predict, is obviously a matter of speculation, not germane to the disposition of the instant petition.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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August, 1958.

APPENDIX

Internal Revenue Code of 1939:

SEC. 26. CREDITS OF CORPORATIONS.

In the case of a corporation the following credits shall be allowed to the extent provided in the various sections imposing tax—

* * * * * *

(h) [As added by Sec. 133 of the Revenue Act of 1942, c. 619, 56 Stat. 798, and amended by Sec. 116 of the Revenue Act of 1943, c. 63, 58 Stat. 21] *Credit for Dividends Paid on Certain Preferred Stock.*—

(1) *Amount of credit.*—In the case of a public utility, the amount of dividends paid during the taxable year on its preferred stock. The credit provided in this subsection shall be subtracted from the basic surtax credit provided in section 27. For the purposes of the credit provided in this subsection the amount of dividends paid shall not include any amount distributed in the current taxable year with respect to dividends unpaid and accumulated in any taxable year ending prior to October 1, 1942. Amounts distributed in the current taxable year with respect to dividends unpaid and accumulated for a prior taxable year shall for the purposes of this paragraph be deemed to be distributed with respect to the earliest year or years for which there are dividends unpaid and accumulated.

* * * * * *

(26 U.S.C. 1952 ed., Sec. 26.)

SEC. 27. CORPORATION DIVIDENDS PAID CREDIT.

(a) [As amended by Sec. 222(a) of the Revenue Act of 1939, c. 247, 53 Stat. 862] *Definition in General.*—As used in this chapter with respect to any taxable year the term "dividends paid credit" means the sum of:

(1) The basic surtax credit for such year, computed as provided in subsection (b);

(2) The dividend carry-over to such year, computed as provided in subsection (c);

(3) The amount, if any, by which any deficit in the accumulated earnings and profits, as of the close of the preceding taxable year (whether beginning on, before, or after January 1, 1939), exceeds the amount of the credit provided in section 26(c) (relating to net operating losses), for such preceding taxable year (if beginning after December 31, 1937); and

(4) Amounts used or irrevocably set aside to pay or to retire indebtedness of any kind, if such amounts are reasonable with respect to the size and terms of such indebtedness. As used in this paragraph the term "indebtedness" means only an indebtedness of the corporation existing at the close of business on December 31, 1937, and evidenced by a bond, note, debenture, certificate of indebtedness, mortgage, or deed of trust, issued by the corporation and in existence at the close of business on December 31, 1937, or by a bill of exchange accepted by the corporation prior to, and in existence at, the close of business on such date. Where the indebtedness is for a principal sum, with interest, no credit shall be allowed under this paragraph for amounts used or set aside to pay such interest. A renewal (however evidenced) of an indebtedness shall be considered an indebtedness.

(b) [As amended by Sec. 132(b) of the Revenue Act of 1942, *supra*] *Basic Surtax Credit.*—As used in this chapter the term "basic surtax credit" means the sum of:

(1) The dividends paid during the taxable year, increased by the consent dividends credit provided in section 28, and reduced by the amount of the credit provided in section 26(a), relating to interest on certain obligations of the United States and Government corporations;

(2) The net operating loss credit provided in section 26(c)(1);

(3) The bank affiliate credit provided in section 26(d).

The aggregate of the amounts under paragraphs (2) and (3) shall not exceed (A) the section 102 net income for the taxable year, in the case of the tax imposed by section 102; (B) the Supplement P net income for the taxable year, in the case of the computations required under Supplement P; or (C) the Subchapter A net income for the taxable year, in the case of the tax imposed under Subchapter A.

* * * * *

(g) *Distributions in Liquidation.*—In the case of amounts distributed in liquidation the part of such distribution which is properly chargeable to the earnings or profits accumulated after February 28, 1913, shall, for the purposes of computing the basic surtax credit under this section, be treated as a taxable dividend paid.

* * * * *

(26 U.S.C. 1952 ed., Sec. 27.)

SEC. 115. - DISTRIBUTIONS BY CORPORATIONS.

(a) [As amended by Sec. 166 of the Revenue Act of 1942, *supra*] *Definition of Dividend.*—The term "dividend" when used in this chapter (except in section 201(*e*)(5), section 204(*e*)(11) and section 207 (a)(2) and (b)(3) (where the reference is to dividends of insurance companies paid to policy holders)) means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made.

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(b) [As amended by Sec. 186(b) of the Revenue Act of 1942, *supra*] *Source of Distributions.*—For the purposes of this chapter every distribution is made out of earnings or profits to the extent thereof, and from the most recently accumulated earnings or profits. Any earnings or profits accumulated, or increase in value of property accrued, before March 1, 1913, may be distributed exempt from tax, after the earnings and profits accumulated after February 28, 1913, have been distributed, but any such tax-free distribution shall be applied against and reduce the adjusted basis of the stock provided in section 113. The preceding sentence shall not apply to a distribution which is a dividend within the meaning of the last sentence of subsection (a).

(c) [As amended by Sec. 147 of the Revenue Act of 1942, *supra*] *Distributions in Liquidation.*—

Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. In the case of amounts distributed (whether before January 1, 1939, or on or after such date) in partial liquidation (other than a distribution to which the provisions of subsection (h) of this section are applicable) the part of such distribution which is properly chargeable to capital account shall not be considered a distribution of earnings or profits. If any distribution in partial liquidation or in complete liquidation (including any one of a series of distributions made by the corporation in complete cancellation or redemption of all its stock) is made by a foreign corporation which with respect to any taxable year beginning on or before, and ending after, August 26, 1937, was a foreign personal holding company, and with respect to which a United States group (as defined in section 331(a)(2),) existed after August 26, 1937, and before January 1, 1938, then, despite the foregoing provisions of this subsection, the gain recognized resulting from such distribution shall be considered as a gain from the sale or exchange of a capital asset held for not more than 6 months.

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(i) *Definition of Partial Liquidation.*—As used in this section the term "amounts distributed in partial liquidation" means a distribution by a corporation in complete cancellation or redemption of a part of

its stock, or one of a series of distributions in complete cancellation or redemption of all or a portion of its stock.

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(26 U.S.C. 1952 ed., Sec. 115.)

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